State of Delaware

Court Modernization Review Committee

Meeting Minutes

This meeting was held on October 10, 2019, in conference room 219 of the Haslet Armory located at 122 Martin Luther King Jr. Blvd S, Dover, DE 19901.

Committee Members Represented or in Attendance:

Director Mike Jackson	Office of Management and Budget
Senator David Sokola	Co-chair, Joint Legislative Committee on the Capital Improvement Program
Senator Brian Pettyjohn	Delaware State Senate, minority party appointee
Representative Debra Heffernan	Co-chair, Joint Legislative Committee on the Capital Improvement Program
Representative Ron Gray	Delaware House of Representatives, minority party appointee
Mike Morton	Controller General
Chief Judge Michael Newell	Delaware Family Court
Secretary Rick Geisenberger	Department of Finance
Tom McGonigle	Delaware Bar Association
Rob Rider	Delaware Prosperity Partnership

Committee Members Not Represented or in Attendance:

Chief Justice Leo Strine	Delaware Supreme Court
Senator Quinton Johnson	Co-chair, Joint Finance Committee
Senator Harris McDowell	Co-chair, Joint Finance Committee

Others in Attendance:

Bill Lenihan	Don Gerardi	Geoff Stewart
Andy Lubin	Ellie Torres	Marcel Ham (via phone)
Michael Svaby	Saul Hernandez	Laird Stabler
Nicole Polite	Evelyn Nestlerode	Jason Smith
Stephanie Scola	Kyle Baranski	

I. Call to order

Director Mike Jackson called to order the Court Modernization Review Committee at 9:10 A.M. on October 10, 2019.

II. Introductions

Director Jackson asked the attendees to introduce themselves.

III. Approval of Minutes

A motion was made by Senator Pettyjohn and seconded by Mike Morton to approve the minutes from the meeting on August 28, 2019.

IV. Presentation on the Public-Private Partnership

Eric Petersen from Hawkins Delafield and Wood presented on the public-private partnership (P3) concept. Hawkins Delafield and Wood law firm provides legal counsel in finance and infrastructure transactions across the country. The law firm's role is as a financial, technical and legal advisor and to help draft the RFP and RFQ with special legislation, if needed. Mr. Petersen provided background on large public P3 projects that are underway or have been completed including Howard County Circuit Courthouse (MD), Long Beach Court Building (CA), and the Javits Convention Center expansion project (NY). The Long Beach Court Building set the template for this type of project. The Howard County Maryland Circuit Courthouse has received three awards for excellence.

Mr. Petersen provided a comparison of traditional contracting and financing with P3 contracting and financing. In the traditional model, the State secures financing, works with a design firm followed by a construction firm. When the building is complete, operations and ongoing maintenance is the responsibility of the State. In a traditional contract, every contract component is separate, including the designing and building process, so there is no opportunity for innovative, collaborative work with the designer and builder. In a P3 model, the State will contract out to a P3 contractor who will form a team with a design-builder, financers, and facilities management who are responsible for operations and maintenance once the building is completed.

Mr. Petersen discussed the financing details of a P3 model. In a P3 model, banks are lending to the P3 contractor and it's pledged to the lender. The P3 contracting will be done by equity sponsor. They take money from an equity fund, and the equity sponsor will own it and will put in about 10% toward the project and the 90% will come from the bank lenders. Lenders will lend to the project company without owning the building because of the public purpose of the building. There are no payments made until occupancy in a P3 model.

Currently there isn't a means in Delaware law to complete a project like this. Special legislation that would allow this type of contract on a competitive proposal basis would be needed. In traditional contracting, price is the sole selection and hinders the competition and design side.

In a P3 contract, after the initial bids, there is a qualifying process to narrow down to three pre-qualified teams who will bid on an RFP. This generates a very effective competition on all aspects of the building proposal. The pre-qualified teams put together the best of the best and provide top quality of the design, testing, how they will build and manage the facilities. Most of the P3 pre-qualified spend about $1M of their own money in pursuit of the contract. The design builder has to absorb most of the cost. Best practice is to pay the unsuccessful proposals $500K, which doesn't fund it fully but shows the State is serious and that someone is going to win the bid. In traditional financing, there would be a cost of 10% to the designer of the project prior to even getting the price proposal. In this process, you want to have the opportunity to have individual meetings with the three pre-qualified teams during the process. This would include a fairness advisor/integrity monitor to sit in, ensuring there is nothing discussed that isn't allowed. However, these companies know they need to have a posture of integrity at every level since the bid is for a public building. The contractors don't want to risk any adverse result in the procurement process.

<u>Advantages of a P3</u>

- Expedited delivery
  - Quicker process for occupancy
- Better value for money
  - Value for money analysis
- Transfer of risks
  - You don't pay until building is completed
  - Performance criteria of these defined elements is transferred to the company with deductions from the service fee if not provided
  - Hand back standards at the end – detailed requirements are included in the contract and typically the building is given back 85% of new
  - All contracts give the ability to terminate the contract (with payment)
- Qualifications Based, Competitive Proposal Selection Process
- Single point of Accountability
- Integrated delivery
- Innovative design
  - Competitive nature produces innovative design
- Best Security for Project Performance
  - Incentive to protect interest
- Life-cycle Focus
  - The cost to not maintain a building for 30 years can be more than the original cost to build it
  - Ongoing capital maintenance is required by the contract
- Engagement of Local Contractors
  - The equity sponsor that forms the project team want to use local contractors knowing that is a factor in public works
  - It can be required as part of the contract or a % requirement and would have to show how to get there

Questions

<u>Do we need a legislative process if we would want to go through with this type of financing?</u>

- Yes, under law it has to be approved by the elected body. Once there is a vote on the contract, they are voting to pay it annually for 30 years, starting at occupancy.

<u>Is the contract valid, binding and enforceable?</u>

- Yes, on the P3 side, if the State gets the fails to make payment during the 30 year term, then action can be taken against the State.

<u>What happens if there is a bankruptcy/dissolving of contracting company?</u>

- If there is a bankruptcy on the contractor, it falls on the P3. The State's risk would only be that the completion of the building would be late, but the State would not be making the payments yet.

<u>Can the P3 sell the loans, change the designer, builder or facilities management contractors?</u>

- There are protections built into the contract. The State is selecting the team as subcontractors, and they don't have the right to replace lenders or contractors until two years after the building is completed.
- Within the contract, the State would be able to keep the P3 contractors accountable by assessing deductions. If there are too many deductions, the lenders would have the right to replace the selected subcontractors, with the State's approval. This alleviates risk.
- There will be technical advisors, a State official and outside specialist for the enforcement of the facilities management contract.

<u>How is the P3 formed?</u>

- P3 is a special purpose LLP solely for the purpose of the project. Equity sponsor will form the entity and controls and is a managing partner. They pull together the team. This is a highly specific and well-developed process leading to the signing of the contract.
- Some examples of companies are international firms like Meridian and Infrared.
- These contracts have been done in USA, Australia, England and Canada.

<u>Do you ever get less than three bids?</u>

- The Howard County project had nine original bids that were narrowed to three pre-qualified bids. The P3 concept is catching on, and there is interest in opportunities like this for companies.
- They would recommend allowing a stipend (as noted above, it is usually $500K) to show that someone is going to get a bid and it allows the State to use the propriety information in the proposal.
- The State can include an affordability ceiling number in the RFP to reserve the right to not award a contract, but it is best to show that the intent is to award a bid to the best value proposer, if it comes in within the affordability range.

<u>Once completed, what incentive does the company have to update the facility and to replace building systems such as to a new energy efficient system?</u>

- In 30 years, the building is turned over at 85% of new. At that point, the State can perform the maintenance or work to negotiate a contract with the company.
    - o This will create an incentive to negotiate updating the building.

  - There are performance guarantees of the building systems.
  - The RFP will require a detailed proposal with the State's maintenance schedule that can be included in the contract.

Is there a pledge of the building itself?

- 90% is financed
  - o The State has the right to approve changes in builder/maintenance contractors.
  - o They can't sell any portions until 2 years from occupancy, and it is subject to the State's approval.
  - o There are provisions to allow the State a reasonable voice in the changes to the projects.
  - o Usually there isn't restrictions on the debt.
  - o In similar projects, lenders tend not to turn over that often.
  - o The facilities management company is vital to the selection process.

Concerns about the financing/credit rating

- The State's bond AAA credit is tax exempt. A project like this for private borrowing will not allow the company to get tax exempt financing.
- This risk is that the State might fall to a BBB rating.
- The cost of capital is less about the tax and more about the credit.
  - o There is a lot of debate about the funding.
  - o In Canada, they treat the payment as debt even though it's not legally debt.
  - o In California, they didn't put it on their balance sheet.

V. Public Comment

There was no public comment.

VI. Adjournment

A motion to adjourn was made by Senator Pettyjohn and seconded by Mike Morton at11:04 a.m.

Respectfully Submitted,

Ronda Ramsburg